

Experts expect compromise to avoid fallout from the 'fiscal cliff'

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(Phys.org)—The image of a "fiscal cliff" may give the wrong impression of the potential fallout should Congress fail to take action by the end of the year on the Budget Control Act. Iowa State economist Dave Swenson described the cliff as more of a step stool.

"It's like you're on level ground and then you stepped in a hole," Swenson said. "It's not the end of the world; it's just an abrupt adjustment."

However, that adjustment will not happen overnight. Swenson said it will take time for the spending cuts to be implemented and there will be an impact on jobs and the economy.

"The economy is so vulnerable right now that the minor adjustment could drag us into a technical recession," Swenson said.

Unlike a recession that is the result of [contractions](#) in the [business cycle](#), Swenson said this would be a "technical" recession because it would be caused by government action.

If Congress does not reach a compromise by the end of the year, it would trigger a 10 percent across-the-board cut on [federal spending](#). The only exemptions to the cuts would be to some social programs, like Medicare and [Medicaid](#). This looming fiscal cliff is tied to the Budget Control Act of 2011 – a compromise between the president and Congress to limit spending after raising the country's debt limit.

Swenson said there are two factors at work that will negatively influence the economy. First, if [tax rates](#) go up, consumers will spend less. According to the Tax Policy Center, the average middle income family would see a [tax increase](#) of about \$2,000.

"At a time when the recovery is being driven by the ability of the average household to consume, it will make it difficult to continue recovery," Swenson said.

Second, the government must cut back on spending which would ultimately result in the loss of jobs. Private businesses that have [government contracts](#) are already scaling back and making adjustments Swenson said. While Iowa's [unemployment rate](#) may be below the national average, there is still a long way to go to recover.

Iowa must add another 60,000 jobs to recover those lost since the start of the recession nearly five years ago, according to employment statistics compiled by Swenson. For comparison, it took just three years to recover the jobs lost during the 1990 [recession](#) and seven years in the '80s.

Political compromise and fallout

Opinions are mixed as to whether Congress will actually allow the country to go over the fiscal cliff. But Steffen Schmidt, University Professor of political science, expects a compromise by the end of the year.

"I don't think they're going to let this go over the cliff. It would be a bad political move," Schmidt said.

While the president and Republican Congressional leaders are making their case to the public, Schmidt said work is going on behind the scenes

to avoid the deadline.

"It's typical of how decisions are made on really, really complicated issues," Schmidt said. "They wait until the last minute to squeeze out every possible concession."

Republicans will have to concede on the issue of a tax increase to generate new revenue, and Schmidt said Democrats will have to agree to cut spending. That means a majority of Republicans, around 95 percent, will have to abandon their pledge to not raise taxes. Schmidt said there is simply no other option.

"[Republicans] have to; if they don't then nothing will get done. We will go over the fiscal cliff unless there's revenue generated," Schmidt said. "If they hold out for no taxes there will be a heavy price to pay in the next off-year election."

Polls show a majority of Americans support some kind of tax increase on the wealthy as well as cuts in spending. Though the clock may be ticking toward the deadline, Schmidt said both sides do not want to give in too soon.

"It's the same as people who play chicken. You don't want to get out of the way at the beginning of the race and be seen as a chicken," Schmidt said. "We want our guy or woman to fight the fight for us right up to the zero hour when the second hand is about to hit midnight. We don't want them to give in early."

Provided by Iowa State University

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